

TELEFÓNICA O2 UK LIMITED RESPONSE TO OFCOM'S CONSULTATION:

**“PROPOSED VARIATION TO AND EXEMPTION FROM BT'S UNDERTAKINGS
UNDER THE ENTERPRISE ACT 2002 RELATED TO FIBRE-TO-THE-
PREMISES AND FIBRE INTEGRATED RECEPTION SYSTEM”**

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OFCOM CONSULTATION: PROPOSED VARIATION TO AND EXEMPTION FROM BT'S UNDERTAKINGS UNDER THE ENTERPRISE ACT 2002 RELATED TO FIBRE-TO-THE- PREMISIES ABND FIBRE INTEGRATED RECEPTION SYSTEM

Introduction

1. Telefónica O2 UK Limited (O2) welcomes the opportunity to respond to the Ofcom Consultation “Proposed Variation to and Exemption from BT’s Undertakings under the Enterprise Act 2002 related to Fibre-to-the Premises and Fibre Integrated Reception System” (the Consultation)¹.
2. As an investor in the UK broadband market² (as well as the UK mobile market and more recently fixed telephony market) with numerous accolades under its belt for its home broadband products³, O2 wishes to see a regulatory regime which builds on the competitive success to date of the UK broadband market and supports sustainable competition for the benefit of UK customers.

Balancing near term pragmatism and long term sustainable competition

3. Ofcom has generally concluded that the vibrancy of the UK broadband market has benefited by the level of competition supported by the regulatory settlement flowing from the Telecoms Strategic Review⁴ (TSR) and the key regulatory components of passive access products such as LLU and the principle of Equivalence of Input (EoI). As regards the Undertakings, Ofcom remarks in its “Impact of the Strategic Review of Telecommunications”⁵ (and elsewhere):

¹ <http://www.ofcom.org.uk/consult/condocs/ftp/ftpcondoc.pdf>

² Telefónica O2 UK’s DSL broadband service reached 527,126 lines at the end of September (+97.4% year-on-year), after recording 70,244 net additions in the third quarter (+34.1% quarter-on-quarter) and 186,260 in the first nine months of 2009.

³ For example: uSwitch Home Broadband Awards 2009: O2 won 9 out of 11 awards; Top10 Broadband Award 2009: Best Rated Home Broadband; JD Power Highest Customer Satisfaction Award 2008; Which? Magazine “Best Buys”: O2’s Home Broadband and Be* brands were Which? Best Buys in 2009.

⁴ <http://www.ofcom.org.uk/telecoms/btundertakings/impact/>

⁵ Impact of the Strategic Review of Telecommunications, Ofcom Statement, 29 May 2009, http://www.ofcom.org.uk/telecoms/btundertakings/impact_srt/

“While not the sole contributing factor to benefits experienced by consumers and businesses, we consider that the Undertakings have played a role in bringing about greater choice and take-up of services, choice of suppliers, products and packages and increased value for money. Competition has played an important factor in the take-up of fixed telecommunications services” [§1.7]⁶

4. Indeed, when Ofcom first began consulting on its approach to Next Generation Access (NGA), O2 made clear that we wanted to see a regulatory regime which enabled efficient and timely investment by all market players that wish to make such investments - not just by the incumbent alone – in NGA.
5. We believe that the regulatory principles established in the TSR and Undertakings remain relevant to NGA. Whilst, some evolution may be appropriate, given the overall benefits of the TSR’s principle of seeking to encourage competition at the deepest level in the network at which it is most likely to be effective and sustainable, we believe that setting a course which significantly departs from that principle presents regulatory risk. As such, we welcome the Consultation’s recognition that Ofcom must be:

“... mindful of the need to maintain the integrity of BT’s Undertakings as a comprehensive solution to the competition concerns identified in our Strategic Review of Telecommunications” [§1.5]⁷

⁶ And as per §4.18 of the Implementation Review: *“The increased take-up of local loop unbundling reflects increased investment by communications providers such as TalkTalk, Sky, Tiscali, Orange and O2 as they have continued to extend the coverage of their networks. Between December 2005 and September 2008 the number of providers using local loop unbundling increased threefold from eight to 24. At the same time, the number of exchanges in which these communications providers have installed equipment increased from 695 to 1,902. This investment resulted in increased choice for consumers as coverage increased significantly. In December 2005, 40% of consumers were covered by one or more LLU providers. By September 2008, this number had more than doubled to 83%. Given the trend towards consolidation in the market, such as the recently announced acquisition of Tiscali UK by Carphone Warehouse, the actual number of LLU operators is likely to reduce to a smaller number of larger scale players who are able to better leverage scale economies thus delivering benefits to consumers”*

⁷ As well as its approach to the variation made early in the year in respect of FTTC: Variation to BT’s Undertakings under the Enterprise Act 2002 related to Fibre-to-the-Cabinet, 11 June 2009, <http://www.ofcom.org.uk/consult/condocs/fttc/statement/>

6. Whilst, at least in the near term, FTTP active solutions may be considered more relevant in some areas and circumstances, we continue to believe that overall, the competitive benefits of passive access products for NGA in relation to supporting effective and sustainable competition remain significant and hence must be safeguarded.

The rationale for Ofcom's current approach to BT's Undertakings in respect of FTTP

7. We note that Ofcom's case for allowing Openreach to control the electronics is based on a number of aspects, including: lack of strong interest from providers other than BT in passive solutions to enable other providers to install their own electronics (see comments elsewhere); the consumer benefits of early deployment (by BT) of FTTP (and FTTC) (which need to be balanced against the longer term benefits for consumers of passive based competition and the fact that active solutions mean that competition runs at the speed of the incumbent's roll out) and the inefficiencies for BT of managing a separation of passive infrastructure and the electronics (yet Ofcom explains: "*...we have not analysed BT's costs estimates in detail*" [§3.33]).
8. In light of this, we have two broad comments in response to the Consultation:
 - Ofcom must take care not to create a self fulfilling prophecy in respect of the future nature of competition – Ofcom needs to avoid foreclosing the options for competition at the deepest level. In short, notwithstanding the near term challenges, we believe that there must be a clear roadmap to passive solutions for FTTP.
 - It is essential that "fit for purpose" GEA and "Voice over NGA" products are developed. In this respect, we believe there must be a "wires only" solution as requested by ourselves and others. We are disappointed that requests for "wires only" via the Openreach SoR process has been rejected by Openreach.

9. We believe that the prospects for competition are dependent on these areas and we discuss our views in greater detail in the remainder of this response.

The opportunities for passive access solutions must not be foreclosed

10. As above, whilst, we note the rationale behind Ofcom's proposed approach⁸ in relation to FTTP – concentrating on active access solutions rather than passive – we believe that Ofcom must take great care not to foreclose options for competition, including competition based on passive access.
11. The benefits of passive based competition have been well recognised in relation to current competitive levels over the course of the debate in relation to next generation access. Ofcom explains in its (FTTC focussed) Statement on Delivering Super-fast Broadband:

“Regardless of the progress made in active product design, limitations will remain on the level of innovation and differentiation supported by active products compared to passive product ...this would suggest that, while the economics of competition based on active products may be more favourable today, propositions based on passive products may nonetheless have an important role to play in the future.” [§1.25]⁹

12. Naturally, the economic and technical challenges for passive based competition in relation to a GPON based solution must be recognised. In practice, at least in the near term, fit for purpose active solutions may well support early competition. However, we believe that it is too early to discount passive options and, as is the case with FTTC (as Ofcom has confirmed¹⁰), we believe that opportunities for competition based on passive access need to be retained in relation to FTTP. Indeed, as per Ofcom's conclusions in relation to FTTC:

⁸ “In light of the benefits that FTTP could offer [to consumers], and the greater efficiency BT could achieve in its deployment if the variation were agreed, we consider that the proposed variation is in the interests of citizens and consumers”. [§1.8]

⁹ http://www.ofcom.org.uk/consult/condocs/nga_future_broadband/statement/statement.pdf

¹⁰ See §5.28, Delivering super-fast broadband in the UK, Ofcom Statement, 3 March 2009, http://www.ofcom.org.uk/consult/condocs/nga_future_broadband/statement/statement.pdf

“[the ruling out of passive access would be] a significant and premature shift in regulatory policy. Passive products form the main basis for competition in current broadband and their presence has arguably been an essential ingredient in the success not just of competition but of the market as a whole.” [§6.9]

13. We note from the responses to Ofcom’s Consultation in respect of varying BT’s Undertakings in relation to FTTC that we are not alone in support for passive solutions:

“Sky and Talk-Talk Group are concerned the variation proposed in our consultation document [FTTC] offered inadequate protection to safeguard competition based on passive products in the long term.” [§3.4]¹¹

14. Accordingly, whilst it may indeed be the case that *“options for competition based on passive inputs for FTTP are at an early stage of development”* [§3.21 of the Consultation], we are concerned that Ofcom risks underplaying interest in passive solutions when it remarks *“there appears to be limited interest, other than from BT, in investing in FTTP infrastructure.”*
15. We are supportive, therefore, of Ofcom’s decision to commission a study to explore the options for competition on GPON-based FTTP deployments [§3.40]. We believe that the framework going forward must require a roadmap to passive solutions and the options for wavelength unbundling should be considered.
16. Nonetheless, overall, if the outcome of the regulatory approach is that appropriate access options are foreclosed then it appears to us that this is likely to give rise to the case for implementing even deeper solutions such as duct and dark fibre access. The European Commission Recommendation on

¹¹ Variation to BT’s Undertakings under the Enterprise Act 2002 related to Fibre-to-the-Cabinet, Statement, 11 June 2009 <http://www.ofcom.org.uk/consult/condocs/fttc/statement/statement.pdf>

NGAs¹² makes clear that NRA's must, in accordance with market demand, mandate access to civil engineering infrastructure (along with the installation of sufficient capacity in civil infrastructure to meet demand) [§§9 -14]. The options for passive based solutions must not be foreclosed.

Fit for purpose active solutions

17. Ofcom's Statement on Delivering Super-Fast broadband makes clear that, given the current focus on active solutions:

“the availability of fit-for-purpose active products is essential for the development of competition in super-fast broadband, particularly in light of the uncertainty around the demand and viability of passive products.” [§5.28]¹³

18. We agree that a “fit for purpose” active product set is essential. We believe that a number of improvements are needed to the current GEA product. We discuss these below.

The GEA product

19. O2 believes that a “wires only” BT product will provide the opportunity for innovation and differentiation in respect of Customer Premises Equipment as well as allowing for providers to build direct customer relationships through own brand CPE supply, installation and maintenance (as opposed to BT branded hardware being delivered by BT). The absence of a wires only product is of concern.
20. Accordingly, there must be a clear route to implement a fit for purpose “wires only” solution. A commitment within the Undertakings to provide such a solution could usefully provide some market certainty.

¹² (Draft) Commission Recommendation on regulated access to Next Generation Access networks (NGA)
http://ec.europa.eu/information_society/policy/ecomm/doc/library/public_consult/nga_2/090611_nga_recommendation_spc.pdf

¹³ Delivering super-fast broadband in the UK, Ofcom Statement, 3 March 2009,
http://www.ofcom.org.uk/consult/condocs/nga_future_broadband/statement/statement.pdf

Delivery of voice services with super-fast broadband

21. As Ofcom points out in the Consultation: *“The prospect of deployment of FTTP has brought to therefore the question of how voice services will be delivered with super-fast broadband products.”* [§3.42]
22. We also agree with Ofcom that: *“the effective evolution of methods for delivery of voice services is important in the development of super-fast broadband”* [§3.44]. Indeed, in its most recent review of the Undertakings¹⁴, Ofcom expressed concern in relation to the clarity over BT’s plans for NGN voice services.¹⁵
23. The Consultation recognises that *“BT’s consumption of an upstream voice product could potentially deliver significant benefits to competition, and hence consumers, by providing a high degree of assurance that the upstream product will be fit-for-purpose”*[§3.52]. We welcome Ofcom’s confirmation that it will consider the options in this respect in the course of the upcoming wholesale local access market review [§3.54].¹⁶
24. In the meantime, Ofcom notes that *“...we interpret the definition of FTTP Active Product on the legal text of Annex 5 to allow Openreach to control and operate, among other things, the Analogue Terminal Adapter (ATA). This electronic function would be required to enable consumers’ existing telephone handsets and home telephone wiring to be used for voice services delivered using digital access to the home, as would be the case with FTTP”* [§3.55].

¹⁴ Impact of the Strategic Review of Telecommunications, Ofcom Statement, 29 May 2009, http://www.ofcom.org.uk/telecoms/btundertakings/impact_srt/

¹⁵ “However, even following the strategy review, there continues to be little clarity over BTs plans for NGN voice services. We are concerned by the uncertainty that this is creating for BTs wholesale customers, as well as the implications for the potential for parallel or notional equivalence, where BT could be using different wholesale inputs to deliver products to end users than some of its larger competitors. Ofcom is considering this issue as part of its continued strategic work on the implications of NGNs for competition, which also includes consideration of the appropriate EOI consumption models” [§1.37]

¹⁶As Ofcom points out elsewhere in its Statement: Impact of the Strategic Review of Telecommunications, Ofcom Statement, 29 May 2009: *“Residential and business consumer outcomes in downstream markets are directly linked to the competitive developments that take place in the upstream markets.”* [§1.11] http://www.ofcom.org.uk/telecoms/btundertakings/impact_srt/

25. We do not see any substantive reason why other communications providers could not provide the ATA and also provide voice and broadband service provided the technology specification is transparent and available. This is also the case for voice delivery via FTTC (as opposed to legacy voice over copper). As above, we believe that it is reasonable for BT to provide a “wires only” product and that the Undertakings should reflect this.

Concluding Comments

26. O2 remains supportive of Ofcom’s approach in its TSR. Further, we welcome Ofcom’s confirmation (in its “Delivering super-fast broadband in the UK Promoting investment and competition”¹⁷) that:

“Ofcom has a central role to play in enabling both investment and competition in super-fast broadband. To do this, we willsafeguard the opportunity for further competition based on physical infrastructure, by facilitating fair opportunities for companies to synchronize their investments with BTs deployments, should reasonable demand arise, and encouraging network design that takes future potential competition into account.” (under “One page summary”)

27. As an investor in the UK broadband market, O2 wishes to see a balanced regulatory framework that enables:

- efficient and timely investment by all market players that wish to make such investments - not just by the incumbent alone - in next generation access (NGA);
- a smooth, appropriately signalled and non-disruptive transition from copper to fibre (including customer migration arrangements) that allows market players to recoup investments and adapt; and

¹⁷ Ofcom Statement, 3 March 2009:
http://www.ofcom.org.uk/consult/condocs/nga_future_broadband/statement/statement.pdf

- the market to work where it can to deliver sustainable competition while ensuring that where there are market failures, the appropriate and proportionate ex-ante regulatory solutions can be executed.
28. In short, a regulatory regime - of which the Undertakings are an integral (albeit voluntary part) - that builds on the success of the broadband market to date and supports sustainable competition into the future. We look forward to working with Ofcom to achieve this.
29. We would be very happy to discuss our comments with Ofcom if that would be helpful.

Telefónica O2 UK Limited
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